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**Trade-related policies and instruments and  
how to use them for resolving commodity problems**

### **Addressing the commodity problematique through trade-related policies**

Note by the UNCTAD secretariat

#### *Executive summary*

Several successful countries have developed by adopting a commodity-based development strategy. However, commodity dependence has more generally been associated with low growth and low levels of economic and social performance, leading many economists to talk about a “resource curse”. This background paper provides an overview of trade-related policies and instruments for addressing commodity problems in commodity-dependent developing countries. It begins with a reminder of the importance of creating an enabling environment for development, in particular for investment, both domestic and foreign, as trade measures on their own are not a sufficient condition for realizing the potential gains from commodity exports. It discusses some specific trade-enhancing measures that can be adopted at the country level to enhance commodity trade, and reviews the opportunities and constraints within the context of the existing multilateral trading system for adopting trade-related policies in order to address commodity problems. It also examines the mechanisms for addressing some of these constraints in the multilateral trading system (MTS). The final section contains some concluding remarks and raises issues which could focus the deliberations of experts.

## Introduction

1. The Accra Accord, in paragraph 93, states that UNCTAD should “assist commodity-dependent developing countries, particularly small commodity producers, in their efforts to develop national commodity strategies, including mainstreaming commodity policies into their national and regional development strategies, build supply-side capacity and attain competitiveness, move up value chains and diversify commodity sectors...” (para. 93(a)); and “Promote intergovernmental cooperation in the field of commodities and consensus-building on...trade-related policies and instruments for resolving commodity problems” (para. 93(b)).

2. A number of countries have succeeded in adopting a commodity-based development strategy (e.g., Australia, Canada, Norway, Chile, Malaysia, Mauritius and Botswana). However, commodity dependence has almost always been associated with low growth and low levels of economic and social performance,<sup>1</sup> notably because of the so-called “Dutch Disease” as well as what has been dubbed the “resource curse”.

3. The resource curse argument has been challenged by a number of studies. In particular, it has been argued that resource endowment is neither “a curse nor a destiny.”<sup>2</sup> Instead, there has been at best “resource disappointment.”<sup>3</sup> Taking the argument further, some studies have demonstrated that causality goes from the quality of institutions to commodity dependence rather than the other way around, placing greater emphasis on the use of resource rents as key to developmental outcomes.<sup>4</sup>

4. In light of this ongoing debate on commodities, this background paper provides an overview of trade-related policies and instruments for addressing the challenges facing commodity-dependent developing countries (CDDCs). It begins with a reminder of the importance of creating an enabling environment for development, in particular for investments by both the public and private sector (both domestic and foreign) in CDDCs (chapter I), as trade policies on their own are not sufficient for reaping the benefits of commodity exports. This is followed by an account of some specific trade-enhancing measures at the country level (chapter II); a review of the opportunities and constraints within the context of the existing multilateral trading system (MTS) for adopting trade-related policies (chapter III) and mechanisms for addressing these constraints (chapter IV). The paper ends with some concluding remarks (chapter V).

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<sup>1</sup> Sachs J and Warner A (1997). Natural resource abundance and economic growth. Working Paper. Center for International Development and Harvard Institute for International Development. Harvard University, Cambridge MA.

Available at [http://www.cid.harvard.edu/ciddata/warner\\_files/natresf5.pdf](http://www.cid.harvard.edu/ciddata/warner_files/natresf5.pdf).

<sup>2</sup> Lederman D and Maloney WF (Eds.) (2007). Natural resources: Neither curse nor destiny. The World Bank, Washington, DC and Stanford University Press, Palo Alto, CA.

<sup>3</sup> Indeed, as Davis put it “to state that resource-rich countries are made worse off for their resources relies on comparison with the unmeasurable counterfactual. It suggests that the Congo, Angola and Nigeria would be doing just fine if natural resources were not found and extracted on their soils.” In Davis GA (2008). Book review of *Escaping the Resource Curse*. Edited by Humphreys M, Sachs JD and Stiglitz JE. New York, Columbia University Press. *Resources Policy*. Vol. 33, Issue 4, December 2008: 240–242

<sup>4</sup> Brunnschweiler CN and Bulte EH (2008). The resource curse revisited and revised: a tale of paradoxes and red herrings. *Journal of Environmental Economic Management* 55 (2008): 248–264.

## I. Creating an enabling environment in commodity-dependent developing countries

5. To thrive, the commodity sector needs an enabling environment that encourages both public and private investment in the sector, including the enhancement of supply-side capacity. That in turn requires good institutions and the integration of commodity policies into national development strategies.

### A. Good institutions

6. “Good institutions” are particularly important, not only for supporting the promotion of commodities but for supporting overall development. The exact definition of good quality institutions remains debatable, but it is generally agreed that good institutions are those that facilitate the development of policies and initiatives, including private business initiatives, that support overall economic development and growth.

#### Style of governance

7. Attempts to pinpoint the factors that led to the remarkable economic performance of newly industrialized economies (NIEs) in East Asia have led to the emergence of the concept of the “developmental State”, which includes some or all of the following characteristics:<sup>5</sup>

(a) A degree of independence from social forces that might potentially distract it from focusing on the country’s long-term development interests in the elaboration and implementation of policies;

(b) Mobilization of a network of social actors supportive of its policies;

(c) Room for “trial and error” policymaking and use of a pragmatic mix of markets and State action;

(d) Strong ideological underpinnings that propel it to assign its resources (human, financial and political) to the pursuit of economic development;

(e) Simultaneous implementation of policy and institutional reforms that encourage both the effective management of “economic rents” and the sequenced exposure of sectors to competitive international economic forces; and

(f) Strong legal and regulatory systems tailored to local needs and conditions.

8. Constraints to making the case for a “strong State” include the limited policy space that developing countries have in the context of the MTS and the predominant neoliberal view of the State as an organization run by politicians and bureaucrats solely motivated by self-interest and with limited capacity to design and execute policies.

9. This view has to be reconciled with findings that suggest that the form of political regime matters in determining economic outcomes.<sup>6</sup> With regards to “resource curse”, empirical analysis suggests that the probability of a “curse” is higher in presidential regimes and in non-democracies. Furthermore, resource firms have been shown to be more

<sup>5</sup> For a review of the literature see UNCTAD (2007). *Economic Development in Africa: Reclaiming Policy Space: Domestic Resource Mobilization and Developmental States*. United Nations publication. Sales No. E.07.II.D.12. New York and Geneva. United Nations.

<sup>6</sup> Persson T and Tabellini G (2004). Constitutional rules and fiscal policy outcomes. *American Economic Review*. 94 (2004) 25–46.

successful in lobbying the government in presidential systems than in parliamentary ones. The failure of sectoral lobbying in agriculture-dependent countries has been explained in part by the diffuse nature of the agricultural sector compared to the clustered nature of mineral resources.<sup>7</sup>

10. All governments in developing countries, including CDDCs, are expected to implement measures aimed at promoting an enabling institutional environment for the business sector. Such measures include reducing transaction costs related to the time needed for conducting business, creating a predictable and stable policy environment by eliminating the probability for policy reversals, and creating a platform for improving the dialogue between the government and sectoral stakeholders.

## **B. Integrating commodities and related sectors in national development strategies**

11. Commodity-related policies have often been neglected when it comes to designing national development strategies, which has resulted in missed opportunities for the commodity sector. Although the objectives of the Enhanced Integrated Framework and the Aid for Trade initiative (see chapter IV) are to assist countries in integrating trade into their development strategies, commodities are seldom explicitly singled out. Commodities are also relevant for the attainment of the Millennium Development Goals (MDGs) – notably goal 1 on poverty and hunger and goal 7 on environmental sustainability – but they are not part of discussions on resource allocation for the achievement of the MDGs. Furthermore, very few of the first-generation poverty reduction strategies specifically addressed the role of commodities in development and in the government’s poverty reduction efforts.

12. There have been a few more recent cases where the role of specific commodity sectors in driving growth is acknowledged. The Government of Malawi, for example, launched the Malawi Economic Growth Strategy (MEGS) in 2004 as part of its drive to link poverty reduction, economic growth and trade and competitiveness issues.<sup>8</sup> The strategy also identified three core sectors (sugar, tea and tobacco) and five development sectors (cotton, textiles, tourism, ministry and agro-processing) as priority areas for support, thus clearly recognizing the key role played by commodities in economic growth and development.

## **II. Trade measures for enhancing competitiveness in commodity-dependent developing countries**

13. Since the establishment of the World Trade Organization (WTO) in 1995, common obligations across all members have defined the MTS. This is particularly so because of the introduction of the principle of “single undertaking”. However, the principle of special and differential (and more favourable) treatment (S&DT) has been built into various agreements, which takes into account the special development challenges of developing, in

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<sup>7</sup> Brunnschweiler CN and Bulte BH (2008). *Op. cit.*

<sup>8</sup> UNCTAD (2006). Malawi and the multilateral trading system: the impact of WTO agreements, negotiations and implementation. Geneva. For examples of diversification strategies undertaken by some commodity-dependent developing countries, see UNCTAD (2009). Integrating commodity policies into development and poverty reduction strategies: success stories, transparency and accountability (TD/B/C.I/MEM.2/3). Note prepared by the UNCTAD secretariat for the Multi-year Expert Meeting on Commodities and Development, 3-5 March 2009. Geneva.

particular, the least developed, countries.<sup>9</sup> Furthermore, the membership of Regional Trade Agreements (RTAs) grants some flexibilities to all countries as these are legitimate under article XXIV (paragraphs 4–10) of the General Agreement on Tariffs and Trade (GATT) 1947 and the “Enabling Clause”. Despite these provisions, many developing countries worry that their development concerns have not been given due consideration in the current multilateral system.<sup>10</sup>

14. The economic performance of CDDCs is heavily dependent on the use of trade and trade-related policy measures aimed at addressing the problems of the commodity sector in order to enhance trade creation. However, these policies, whether at the country or regional level, have to be consistent with the general WTO disciplines, including the S&DT provisions. As discussed below, this is not without its constraints, thereby reducing the room for manoeuvre for some CDDCs in terms of the employment of trade policies which best respond to their special circumstances. This notwithstanding, CDDCs have implemented a variety of trade policy measures in an effort to address their commodity problematique. Some of these are discussed below

## A. Trade facilitation measures

15. Sub-Saharan Africa is home to half of the world’s landlocked countries with Chad, Niger, Zambia and Zimbabwe being classified among the countries with the longest distances from the nearest seacoast (in excess of 2,000 km). Against this background, geographical remoteness and the resulting high transport costs are considered to be among the key constraints to the inability of these countries to be competitive in regional and international markets.<sup>11</sup>

16. Given these geographic constraints, trade facilitation is key to improving the external competitiveness of many developing countries. There are currently a number of trade facilitation initiatives in Africa and elsewhere. These initiatives include the Sub-Saharan Africa Transport Policy Programme (SSATP), a partnership of 35 African countries, 8 regional economic communities, 3 African institutions – AU/NEPAD and UNECA – national and regional organizations as well as international development partners. The SSATP’s goal is to ensure that “transport plays its full part in achieving the developmental objectives of sub-Saharan Africa: poverty reduction, pro-poor growth, and regional integration”. The programme is funded by a plethora of bilateral and multilateral donors including the European Commission, the Islamic Development Bank, the African Development Bank and The World Bank.

<sup>9</sup> Some of the S&DT measures are also contained in the “Decision on Measures in Favour of LDCs”, annexed to the Final Act of the Uruguay Round. The implementation of these provisions has not been without problems, though. In particular, there has been a lack of political will to fully activate or implement S&DT provisions. Thus “policy flexibility”, which is the intended objective of these provisions, has not been provided in a meaningful way for developing countries. There are also many other instances of imbalance and unfairness within the multilateral trading system, which fall outside the scope of this note.

<sup>10</sup> See, for example UNCTAD (2010). Recent developments in key commodity markets: trends and challenges (TD/B/C.I/MEM.2/7). Note prepared for Multi-year Expert Meeting on Commodities and Development. 24–25 March 2010. Geneva.

<sup>11</sup> UNCTAD (2006). *Op cit.*

17. As part of its regional integration theme, the SAATP aims to give priority to transit corridors serving landlocked countries. The priority corridors are as follows:<sup>12</sup>

(a) Northern and Central corridors providing access to Uganda, Rwanda, Burundi and Eastern Democratic Republic of the Congo through Ports of Mombasa and Dar es Salaam respectively;

(b) The Djibouti-Addis Ababa corridor serving Ethiopia;

(c) The North-South corridor linking Botswana, Democratic Republic of the Congo, Malawi, Zambia and Zimbabwe to the Port of Durban;

(d) The Dar es Salaam corridor serving Malawi, Zambia and the Democratic Republic of the Congo;

(e) The Central Africa and Congo River corridors serving Central African Republic and Chad;

(f) The West African corridors linking Burkina Faso, Mali and Niger to Lomé and Tema (Accra) port.

18. Other key conditions to countries' ability to be competitive include predictability in delivery, cost-effectiveness of international logistics services and efficiency of cross-border operations.

## **B. Standards compliance**

19. Standards compliance is important both for regional and international markets. LDCs' lack of capacity in fulfilling these stringent requirements has weakened their export competitiveness and their ability to seize market opportunities. South Africa, for example represents the most important horticultural market in Southern Africa for neighboring countries such as Mozambique. However, compliance to stringent standards remains a challenge especially for small-scale farmers. Meeting these standards would represent a great opportunity for local suppliers as it has also been argued that doing so would also enable Mozambican farmers to exploit market opportunities in Europe.<sup>13</sup> For that to happen, suppliers would need to comply with private commercial standards such as GLOBALGAP (formerly known as EUREPGAP).

20. CDDCs in the West Africa region also face major challenges in standards compliance. As part of its capacity-building activities, UNCTAD has designed and is implementing a project aimed to assist producers' associations and export groups in Guinea to comply with SPS requirements and retailer's agri-food safety standards. The project was launched in November 2005 with funds from the Standards Trade Development Facility and is pending due to the current political situation in Guinea.<sup>14</sup>

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<sup>12</sup> World Bank (2008). Sub-Saharan Africa Transport Policy Program (SSATP). SSATP Annual Report 2007. SSATP Report No 06/08/ AR07. Washington DC.

<sup>13</sup> UNCTAD (2008). Linking African Small Producers to Large Distribution Networks: Enhancing Capacity of Mozambican Producers to Supply the South African Market. Geneva.

<sup>14</sup> Completed activities so far include (a) the development of training materials for modules focused on quality management, food safety and ways to meet the growing exigencies of markets; (b) the creation of a public inspection force of 10 inspectors drawn from key national agencies; (c) the development and implementation of Good Agricultural Practices (GAP) and other safety assurance systems (such as HACCP, ISO 9000, ISO 22000, etc.) in three selected pilot farms, seeking certification; and (d) the contribution to national certification capacity by establishing links with an

## C. Increasing value addition

21. Africa remains the continent with the highest proportion of countries dependent on primary commodities, although paradoxically, it has fallen behind other developing regions of the world in the export of non-fuel primary commodities. As such, the secular decline in real commodity prices and the recent price hikes have exposed sub-Saharan Africa's lack of competitiveness and the need for moving up the value chain. In the strategy to move up the value chain, a propitious environmental climate, reliable and cheap electricity, an industrial free zone, economies of agglomeration are among the most important components of a policy package.

22. Many countries have designed investment codes, but research suggests that an investment code is no panacea for attracting foreign direct investment (FDI), and that other factors such as skill levels, infrastructure and, high level political leadership and commitment are perhaps more important to investment promotion. The last factor is best illustrated by the case of the textiles and apparel sector in Ghana (box 1).<sup>15</sup> Thanks to the successful implementation of an investment incentive scheme, Ghana is considered to be the top performer in West Africa's cotton sector.

### Box 1. Ghana's strategy for value addition in the cotton, textiles and apparel sector

Under the Presidential Special Initiative (PSI), Ghana has set up an investment incentive scheme that particularly favours the garment manufacturing industry. The PSI has a three-tier strategy:

- (a) Attracting 10 large-scale foreign garment/textile manufacturers to locate/relocate their factories in Ghana's Export Processing Zone;
- (b) Building the supply capacities of 100 medium-sized Ghanaian garment companies to export; and
- (c) Creating a large pool of small-scale local subcontractors and secondary suppliers.

Apart from the export free zone status with generous exemptions from taxes (10 years exemption on profits), duties (if exporting over 70 per cent of production) and levies, and unrestricted capital and profit repatriation, garment manufacturers have fast-track access to sites for factory buildings. Rentals and electricity costs are partly subsidized. In this regard, they have already created a 178-acre garment and textile site within Ghana's main export processing zone located at the port city of Tema. The site can accommodate 112 factories, six of which have already been built and occupied. A hospital is to be added.

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internationally accredited certification laboratory and national public/private auditors working for the Guinea CERE laboratory. For further details on this project, see UNCTAD (2009). A model for the development of a public-private safety control system for the horticultural sector in Guinea, West Africa. STDF/SPS Project No. 65. Geneva.

<sup>15</sup> USAID (2006). Adding value to West African cotton: Assessment of the cotton-textile-apparel value chain. WATH/Accra Technical Report No. 1.

In Accra, there is another, more congested export processing site for garment manufacturers, where four companies are located, and three additional factories are being built. Each can accommodate 300–400 sewing machines, plus store rooms, cutting tables, ironing tables/machines, and inspection and packing areas.

The PSI has also invested \$1.2 million in a modern Clothing Technology and Training Centre to train a large pool of employable manpower at all levels for the garment industry (from pattern makers, cutting and sewing through to quality control, supervisory and managerial levels). They have the capacity to train 10,000 people per annum. Five hundred trainees have completed the training, although most company managers claim that significant additional training in-house is required before companies can start working on orders. Based on the number of factories going up and machines coming into Ghana, the number of trained workers will need to increase to approximately 3,500 people. The recent announcement of a factory relocation from Kenya will mean that 2,000 additional people will need to be trained within the next six months.

*Source:* USAID (2006). Adding value to West African cotton: Assessment of the cotton-textile-apparel value chain. WATH/Accra Technical Report No. 1: 17.

## 1. Reliable and affordable electricity

23. Reliable and affordable electricity is important for attracting investment into higher value added activities. There are large disparities in the cost of electricity connection across countries.<sup>16</sup> In addition to cost consideration, reliable supply also matters for ensuring the proper functioning of productivity-enhancing trade technical devices. The use of automated customs systems in a number of African economies for example (e.g. Ghana, Kenya and the United Republic of Tanzania) has been hampered by the lack of access to uninterrupted power supply and high-speed internet connections.<sup>17</sup>

24. With regards to the commodity sector, low electricity costs can play an instrumental role in the competitiveness of specific industries. In the mid-1990s, for example, Gencor, a South African company, chose Mozambique as a basis for expanding its aluminium production. Given that electricity is a major component of the cost of aluminium production, the motivation was partly motivated by the company's comparative advantage of having one of the lowest electricity costs per unit of any smelter in the world,<sup>18</sup> thus allowing it to be competitive on the world market.

<sup>16</sup> World Bank (2006). *Op. cit.*

<sup>17</sup> World Bank (2006). *Op. cit.*

<sup>18</sup> Pretorius L (2001). Industrial free zones in Mozambique: A case study of the Mozal aluminium smelter. Mimeo. Centre for Southern African Studies. University of Western Cape.



## 2. Industrial Free Zones

25. IFZs are industrial zones that generally offer tax exemptions and other fiscal and infrastructural advantages to local and foreign companies involved in the export of processed goods. Foreign companies established in IFZs are usually required to provide assistance to local businesses in acquiring technology, machinery and skills. They are also expected to generate direct job creation as well as forward linkages through the contracting of local downstream processing plants. The best known case is Mauritius' free trade areas. Other examples include Cameroon's Industrial Free Zone, highlighted in box 2, which has been credited for attracting investments to the mineral sector.

## 3. Clusters

26. Although clusters are credited with providing a propitious environment for a sector's development, there are a limited number of clusters of commodity-based manufacturing in sub-Saharan Africa. A recent study listed cut flowers in Kenya, textile and clothing respectively in Mauritius and in South Africa and wine in South Africa (see table 1). Research suggests that cluster formation is subject to the availability of a number of enabling conditions. In the case of Kenya's cut flowers and South Africa's wine, natural endowments such as favourable climatic conditions, abundant land and water resources have contributed to the concentration of a number of farms in the same area. Firms located in clusters can benefit from externalities – e.g. shared facilities such as warehouses as well as any other public-funded infrastructure. They also benefit from reduced transaction costs due to the proximity of many components of specific value chains.

Table 1

### Products and location of clusters in sub-Saharan Africa

Products	Location	Number of firms
Cut flowers	Lake Naivasha, Kenya	24
Textile and clothing	Mauritius	260
Textile and clothing	South Africa	327
Wine	South Africa	+ 340

*Source:* Adapted from Zeng DZ (2006). Knowledge, technology and cluster-based growth in Africa: Findings from 11 case studies of clusters in Africa. WBI Development Study. World Bank, Washington DC: 4.

27. Foreign investment also plays a key role, as illustrated by the case of the cut-flower cluster in Kenya, where total investment into the flower industry from 2002 to 2004 was \$200 million–\$300 million. Top investors come from Israel and the Netherlands. The origins and current state of the cluster are described in box 2.

### Box 2. The cut-flower cluster in Kenya

Kenya's flower cluster emerged in the 1970s alongside the horticultural subsector, which also includes fruits and vegetables. Cut flowers, fruits and vegetables share some similar characteristics in terms of growing conditions and perishable nature of product.

Growth of the cut-flower cluster started to pick up in the 1980s, when the leading exporters started commercial rose cultivation. However, the industry was characterized by low value and simple open field flowers with limited assortment in the 1980s. In the 1990s, the industry shifted to higher-value

flowers grown in greenhouses. There was a marked increase in production, with growers increasing their planting area by about 250 per cent. By 1999, Kenya was exporting about 100,000 tons of horticultural produce, a 10-fold increase from 1975, with cut flowers accounting for about 37 per cent of this volume.

In recent years, the sector has benefited from a surge in new foreign investment, particularly from Israel and the Netherlands, and many of the dominant flower producers are owned and managed by expatriates. According to a World Bank estimate, the total investment into the flower industry from 2002 to 2004 was \$200 million–\$300 million. The continued investment in the sector has further upgraded the cluster's technology, production skills and market know-how.

Today, Horticulture is Kenya's largest and fastest-growing export goods cluster, and cut flower exports have increasingly gained a strong footing as one of Kenya's main source of foreign exchange earnings. In 2005, the horticulture exports were worth \$590 million and accounted for about 18 per cent of Kenya's total goods exports. Within this horticulture category, Kenya's cut-flower cluster earned \$304 million and accounted for about 60 per cent of horticulture exports, with roses accounting for 63 per cent of total cut-flower exports.

*Source: Hornberger K et al. (2007). Kenya's cut-flower cluster. Microeconomics of Competitiveness: 17.*

28. Clusters facilitate the creation of a knowledge network that allows firms to benefit from different forms of inter-firm linkages such as subcontracting and easier linkages with consumers and suppliers. Subcontracting, for example, allows smaller firms to sell to larger firms that benefit from the certification to sell to the European market. Subcontracting also allows larger firms to rely on smaller firms to supply varieties for which they do not wish to engage in because of extra operational costs. Other cluster advantages include knowledge acquisition through cooperation with foreign firms.

29. Clusters thrive best when the general conditions related to an enabling business environment exist, namely basic infrastructure, a conducive institutional regime, a skilled labour force and close public–private partnership.

### **III. Opportunities and constraints in the MTS**

#### **A. Regional Trade Agreements**

30. By December 2008, 421 RTAs had been notified to GATT/WTO. In addition to the promotion of trade liberalization and deeper integration among member countries, RTAs play a key role in the improvement of infrastructure, the harmonization of standards and customs procedures, in generating a strong political will for implementing reforms and in strengthening the region's bargaining power in multilateral trade negotiations. In East and Southern Africa for example, the Southern Africa Development Community (SADC) tends

to focus on infrastructural constraints whereas the Common Market for Eastern and Southern Africa (COMESA) tackles harmonization of standards and customs procedures as well as trade facilitation.

31. By removing infrastructural bottlenecks, RTAs can be instrumental in improving the functioning of intraregional commodity trade. Furthermore, given their unique regional expertise, RTAs can play a leading role in the design of regional commodity strategies. In doing so, they can also give more political visibility to commodity issues as in the example of the African Union's 2005 Arusha Declaration on African Commodities.

32. RTAs can legislate and enforce steps towards the establishment of a region-wide legal and regulatory framework in areas related to commodity marketing, e.g. commodity exchanges and warehouse receipt systems. They also have the expertise to design and enforce sector-wide commitments. For example, the Comprehensive Agricultural Development Programme that the African Union has adopted as part of the New Partnership for Africa's Development (NEPAD) is currently implemented in about two dozen countries, eight of which have already reached the goal of allocating 10 per cent of national budget to the sector.

33. It should be mentioned, however, that there has not been a comprehensive treatment of agricultural commodities in most RTAs relative to the treatment of manufactures.<sup>19</sup> Furthermore, in circumstances where RTAs have extended preferential treatment to agricultural products, this has been limited and most often excludes products considered "sensitive"

34. RTAs have also been afflicted by a number of constraints. First of all, in Africa, the trade creation potential of RTAs has been challenged due to the lack of product complementarities among members. There are, for example, findings demonstrating that asymmetric complementarity in COMESA/SADC implies that the more developed economies of Kenya, Egypt and South Africa benefit from marketing their exports in COMESA/SADC whereas other member countries cannot find significant markets there. Secondly, in the case of Africa, multiple RTAs have overlapping memberships, therefore resulting in competing and sometimes conflicting programmes of trade liberalization, high administrative and financial costs as well as stretching already scarce trade negotiating capacities.

35. In a bid to address these challenges, the three Regional Economic Communities (RECs) in East and Southern Africa – COMESA, the East African Community (EAC) and SADC – joined forces in a Tripartite Initiative in 2005 and since then have agreed to work together in order to achieve a congruence of activities. Furthermore, a road map has been set for the achievement of a Tripartite Free Trade Area (FTAs) by January 2012. Estimates show that exports among the 26 Tripartite countries increased from \$7 billion in 2000 to \$27 billion in 2008, and imports expanded from \$9 billion in 2000 to \$32 billion in 2008, thus illustrating the potential for merging the three FTAs<sup>20</sup>.

36. The tripartite arrangement has also committed to more coordination and harmonization on EPA negotiations and multilateral negotiations including the WTO Doha Development Round Negotiations. And finally, joint infrastructure initiatives include the establishment of a Joint Competition Authority (JCA) on Air Transport Liberalization, a

<sup>19</sup> See, for example, UNCTAD (2009). Integrating commodity policies into development and poverty reduction strategies: Success stories, transparency and accountability (TD/B/C.I/MEM.2/3). Note prepared by the UNCTAD secretariat for the Multi-Year Expert Meeting on Commodities and Development. 3-5 March 2009. Geneva

<sup>20</sup> <http://www.comesa.int>.

joint programme for the implementation of a single seamless airspace and a joint programme for the implementation of an accelerated, seamless interregional ICT Broadband Infrastructure network.

37. Although actual implementation remains a challenge, these initiatives aimed at promoting trade between members are bound to further promote intraregional trade in commodities as well as create an enabling environment that will assist CDDCs in moving up the value chain. In particular, it may help in formalizing the huge informal cross-border trade in agricultural commodities (especially in foodstuffs), and therefore create opportunities for enhancing trade in these products.

## **B. The Doha Development Agenda**

38. The Doha Development Agenda (DDA) launched in November 2001 includes new negotiations as well as the commitment to work on the implementation of the present agreements from the Uruguay Round of negotiations. Following ministerial discussions in Cancun (2003), Hong Kong, China (2005) and in Geneva (2004, 2006, 2008, 2009), the round is still not concluded.

39. The DDA is expected to result in increased trade opportunities for least developed countries (LDCs), thanks to duty-free and quota-free access to developed and developing country markets, sharp reductions in agriculture subsidies in rich countries, the elimination of export subsidies, and the disciplines on fishery subsidies. It is the first round to focus strongly on agricultural trade liberalization. The general expectation is that trade liberalization will result in welfare gains for developing countries.

40. Notwithstanding these potential advantages, many developing countries face difficulties in undertaking negotiations as well as in the actual implementation of existing trade agreements. Other constraints include tariff escalation, which limits the benefits of undertaking a strategy of vertical diversification by low-income CDDCs. Concerns have also been expressed about the unfairness of some of the negotiated disciplines, particularly the manner in which they are being applied or interpreted.

41. Many studies suggest that the welfare gains from trade liberalization resulting from the DDA, although positive, would be limited for the majority of developing countries. It appears that only a minority of countries would witness a reduction in their poverty headcount due to partial agricultural reforms under the postulated Doha scenario. In line with earlier findings that show the limited poverty impact of the DDA,<sup>21</sup> some analysis insists that “the full reforms [i.e. DDA reforms combined with domestic trade agricultural trade liberalization policies in developing countries] are almost twice as poverty-friendly as the Doha reforms”.<sup>22</sup>

42. However, the estimates of welfare gains from the DDA perhaps risk underestimating the importance of trade liberalization in key commodities for poverty reduction in CDDCs. Cotton, for example, is a case in point. United States subsidies to cotton growers, for example, are estimated to amount to about \$3 billion a year, more than twice all United States foreign aid to sub-Saharan Africa in 2001, thus illustrating the sizeable trade distortions suffered by the sector. In 2003, Benin, Burkina Faso, Chad and Mali (the “cotton 4”) raised the profile of cotton in the DDA by launching the so-called cotton

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<sup>21</sup> Ivanic M (2006). The effects of a prospective multilateral trade reform on poverty in developing countries. Chapter 14 in Hertel TW and Winters LA (editors). *Poverty and the WTO: Impacts of the Doha Development Agenda*. World Bank and Palgrave.

<sup>22</sup> Hertel T, Keeney R, Ivanic M and Winters A (2008). Why isn't the Doha Development Agenda more poverty friendly? GTAP Working Paper No. 37.

initiative. The initiative emphasized the damage that subsidies provided by Organization for Economic Cooperation and Development (OECD) countries cause to cotton-producing developing economies, and asked for the establishment of a compensation fund. Following their request, cotton has become a key part of the negotiations on agriculture. However, there has been no substantial progress on the trade aspects of cotton, given that they are an integral part of the overall agricultural negotiations.

43. Other sectors, such as rice and sugar, have also suffered from trade distortions resulting from developed countries' subsidies, although the situation for sugar, for example, has changed with the implementation of new Economic Partnership Agreements (EPAs).

### C. Preferential market access

44. Fifty LDCs benefit from special preferences from developed countries. Special and Differential Treatments include (a) the European Union's (EU's) Everything But Arms trade arrangement with LDCs; (b) the Cotonou Agreement signed between the EU and the African, Caribbean and Pacific (ACP) Group of States in 2000, thus succeeding to the Lomé Convention and Protocols; (c) the United States African Growth and Opportunities Act (AGOA), enacted in 2000, which extends trade preferences to sub-Saharan African countries; (d) the United States' Caribbean Basin Initiative (CBI); and (e) Canada's scheme for Caribbean countries (CARIBCAN).

45. Given the historical ties between ACP countries and some European countries, agreements between the EU and ACP countries have often taken centre stage in the debate on preferential market access. As part of the Cotonou Agreement, the concerned parties have committed to enter into negotiations on "EPAs, a separate set of individual bilateral treaties between the EU and the participating ACP countries." EPAs are expected to provide specific rights and obligations to each of the following clusters of countries: West Africa, Eastern and Southern Africa (ESA), Central Africa, SADC, the Caribbean and the Pacific.

46. Negotiations on EPAs were initially expected to be completed by September 2007. However, in some countries, the controversy raised by the loss of customs revenue and a potential flood of EU imports, among other concerns, resulted in campaigns to stop their signing. A series of studies that have investigated the potential impact of EPAs on ACP countries' highlighted possible employment and welfare losses, even if trade were to increase.<sup>23, 24</sup> Many countries have nonetheless agreed to sign interim EPAs, whereas Senegal swore not to sign until development concerns were given due consideration. Table 2 gives an account of the state of EPAs as of early 2009.

<sup>23</sup> Morrissey O and Zgovu E (2007). The impact of economic partnership agreements on ACP agriculture imports and welfare. CREDIT Research Paper No 07/09. University of Nottingham.

<sup>24</sup> Milner C, Morrissey O and Zgovu E (2009). EU-ACP Economic Partnership Agreements and ACP integration. CREDIT Research Paper No 09/05. University of Nottingham.

Table 2

**State of Interim Economic Partnership Agreements as of January 2009****Regions and state of progress**

**Central Africa:** A regional agreement with Cameroon (other countries in the region finally opted not to join the agreement)

**Southern Africa (SADC region):** A regional agreement with Botswana, Lesotho, Swaziland, Mozambique and Namibia

**West Africa:** Individual agreements with Côte d'Ivoire and Ghana

**East Africa:** A regional agreement with the East African Community (Kenya, Uganda, United Republic of Tanzania, Rwanda and Burundi)

**Eastern and Southern Africa (ESA region):** A regional agreement with Comoros, Madagascar, Mauritius, Seychelles, Zambia, Zimbabwe (but with individual market access schedules)

**The Pacific:** A regional agreement with Papua New Guinea and Fiji (but with individual market access schedules)

*Source:* Adapted from European Union. 2009. Fact sheet on the interim Economic Partnership Agreements: An overview of the Interim Agreements. Brussels.

47. Recent developments include the signing in August 2009 of an interim EPA between the EU and countries from the ESA region. The list comprises Mauritius, Seychelles, Zimbabwe and Madagascar.<sup>25</sup> The agreement allows these countries immediate and full access to EU markets (with transition periods for rice and sugar), together with improved rules of origin. In exchange, ESA countries will gradually open their markets to the EU over the next 15 years. Exceptions include sensitive products such as milk, meat, vegetables, textiles, footwear and clothing.

#### IV. Mechanisms for addressing the constraints to the MTS

48. LDCs' stagnating share of world exports and their limited capacity to broaden their export product base have highlighted the need to assist them in addressing institutional constraints as well as poor infrastructure that still undermine their capacity to benefit fully from trade. As a result, in recent years, the international development community has provided increased resources for trade-related technical assistance.

##### Trade-related technical assistance

###### 1. Technical assistance needs

49. Most CDDCs have limited capacities for trade negotiation. In addition to building up their own negotiation capability through technical assistance, such countries also need to build alliances with others in similar positions with similar interests. In the case of EPA negotiations, for example, countries such as Malawi, which are still hesitant in signing the interim EPA, could join forces with other ACP countries also interested in an EPA with the EU.

50. With regards to WTO negotiations, the African Group and ACP countries in general have demonstrated their capacity to press for their joint interests to be taken into account. However, regular monitoring and feeding of information between central governments and

<sup>25</sup> Zambia and Comoros will sign at a later date and Djibouti, Ethiopia, Eritrea, Malawi and Sudan are among the other likely beneficiaries of this comprehensive deal.

their Geneva-based negotiators remain a challenge, thus creating the need for specific technical assistance.

51. Technical assistance is also needed in the areas of marketing as well as in the actual implementation of the WTO agreements, including policy and legal advice. The need for better coherence of trade-related technical assistance has been addressed in the context of the Integrated Framework and the Aid for Trade initiative.

## **2. Joint Integrated Technical Assistance Programme**

52. JITAP is a programme through which UNCTAD, WTO and the International Trade Centre UNCTAD/WTO (ITC) coordinate their responses towards building trade-related human, entrepreneurial and institutional capacities in Africa. JITAP began its implementation phase in March 1998 using resources from the Common Trust Fund with contributions from a wide range of donors. As of 2005, 16 countries were benefiting from the programme's capacity-building activities with a clearer formulation of export strategies. Intervention areas included cassava, hides and skins, textiles, fish products, and fruits and vegetables.<sup>26</sup>

## **3. The Enhanced Integrated framework**

53. The Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries, more generally known as the Integrated Framework (IF), was officially launched by six multilateral institutions (the International Monetary Fund, ITC, UNCTAD, United Nations Development Programme (UNDP), World Bank and WTO) in 1997. The IF was established in order to support LDC governments in trade capacity-building as well as assist them in integrating trade issues into overall national development strategies. The IF also aims to assist in the coordinated delivery of trade-related technical assistance based on the principles of country ownership and partnership.

54. In 2003/2004, an evaluation of the IF showed that trade-related reforms were still not mainstreamed into national development strategies. The evaluation also revealed that donor coordination was weak and that there was limited funding available for supporting priority projects. The Enhanced Integrated Framework (EIF) was subsequently designed to address these limitations.

55. The EIF has three interrelated objectives: increased in-country productive capacity, improved global governance and increased finance. The EIF has become a key mechanism in assisting LDCs to access additional Aid for Trade resources. It does so by enabling LDCs and donors to match up the demand and supply sides through a procedure for mapping out and prioritizing key needs for trade-related assistance and capacity-building, encompassing trade infrastructure, supply and productive capacity. LDCs' demands are then communicated to the donor community in order to widen funding sources beyond those available in the framework's own Trust Fund. By ensuring better coordination of all donor assistance, the EIF is considered to be a concrete translation of the Paris Declaration on Aid Effectiveness.

## **4. Aid for Trade initiative**

56. The Aid for Trade (AfT) initiative was launched at the WTO Ministerial Conference in Hong Kong, China, in 2005. Its objective is to assist developing countries, particularly LDCs, develop the necessary trade-related skills and infrastructure for increased competitiveness in the global economy. The July 2009 review of the Aid for Trade

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<sup>26</sup> [www.jitap.org](http://www.jitap.org).

initiative showed an increased profile of trade in the development strategies of partner countries as well as an increased donor response in activities for building trade capacity. The latter is evidenced in the year-on-year increase by approximately 10 per cent in the flow of Aid for Trade resources since 2005.<sup>27</sup> However, an assessment of Aid for Trade activities in the Africa region also shows that, although the amount of Aft to Africa grew by an average 12.8 per cent between 2002 and 2006, the countries that needed it most appear to be the ones that received the least.<sup>28</sup> Notwithstanding the initiative's mixed results, it has provided the resources for a number of activities with a direct impact on the commodity sector

## 5. WTO's dispute settlement mechanism

57. The "dispute settlement mechanism" is the official framework for resolving trade disputes within the institutional setup of WTO. These disputes often arise when "one country adopts a trade policy measure or takes some action that one or more fellow WTO members considers to be breaking the WTO Agreements; or to be a failure to live up to obligations". Issues under dispute span a wide range of categories. With regards to commodities, dispute issues have included rice, fisheries, fruits and vegetables, as well as more processed products such as textiles and steel. LDCs get special consideration as developed countries are mandated to "exercise due restraint in raising matters involving a least developed country and in seeking compensation from or the right to retaliate against a least developed country".<sup>29</sup> However, a look at WTO's list of dispute cases also reveals that LDCs do not figure prominently among complainants or third parties. For example, textiles cases only involve either major developed countries or a developed versus a developing country or two developing countries. Out of the 18 cases listed, none involved an LDC as one of the concerned parties, with the exception of Bangladesh. This lack of engagement is partly due to the expensive costs associated with dispute settlement proceedings. Therefore, although the WTO secretariat conducts special training courses for interested members concerning dispute settlement procedures and practices, there is no provision for assisting LDCs in the costs that such procedures generate.

58. Resource-constrained developing countries can request assistance from the Agency for International Trade Information and Cooperation (AITIC), whose mandate is to provide support for their effective participation in WTO and in the MTS. The agency's activities are funded by sponsoring members and other voluntary contributions.

## V. Concluding remarks

59. The MTS is defined by the existing WTO Agreements and any agreement resulting from ongoing (and future) trade negotiations within the framework of WTO. As such, trade policies, including those relating to commodities, should be consonant with these agreements. However, for the least developed countries and other poor WTO member countries, there are the special and differential treatment measures or provisions annexed to these agreements which grant them some flexibility in trade policies. RTAs also grant some flexibility to all countries.

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<sup>27</sup> OECD and WTO (2009). *The Aid for Trade at a glance 2009: Maintaining momentum*. Paris and Geneva.

<sup>28</sup> UNECA (2009). *Global review on Aid for Trade 2009: Issues and state of implementation in Africa: Does supply meet demand ?* Addis-Ababa.

<sup>29</sup> [www.wto.org](http://www.wto.org).



60. Nonetheless, CDDCs do not appear to have taken advantage of these flexible provisions to design trade-related policies that specifically address their commodity problematique at the national or national levels. Reasons for this include, among others, the lack of political will to enforce or implement of these S&DT provisions and the fact that commodities and commodity-related trade policies have rarely been prioritized within the context of national development strategies or RTAs.

61. Commodity-related problems raise systemic issues that need to be addressed through coherent and concerted actions at the national level, and regional and multilateral levels. Also, emerging issues (such as the “financialization” of commodity markets) point to emerging complexities, whereby trade, finance and investment are increasingly interconnected. However, it appears that developments in the rules and institutions that govern the global commodity economy have not kept pace. That is, proportionate institutional innovation and legislation have not been taken at the multilateral level to deal with the increasing integration between trade, investment and finance. This has impaired multilateral institutional capacity to address structural and systemic issues, shifting responsibility unduly on to the domestic level. This has hindered the capacity to formulate effective strategies and policies to respond to the challenges of global commodity markets, in particular dealing with the persistent structural imbalances in the global commodity economy.

62. The “financialization” of commodity futures trading also raises pressing regulatory issues and probably calls for a “smart regulatory” intervention. The need for tighter regulation has been discussed mainly in relation to speculative position limits<sup>30</sup> and to the “swap dealer loophole”.<sup>31</sup> The questions that the current financial crisis poses go beyond better regulation of commodity exchanges. In addition to regulatory issues, the crisis has revived attention to direct intervention in case of destabilizing speculation, including through buffer stocks schemes.

63. These new developments engender several pertinent issues which experts may want for provide some policy directions:

(a) What are the mechanisms for integrating commodity sector policies into national and regional development strategies?

(b) What should be the response at the regional and multilateral levels to this growing interconnectedness between commodity trade, finance and investment?

(c) How do we address the structural causes of the ongoing crises in the commodity sector?

(d) Is it possible to curb the possible role of financial investors in exacerbating price movements away from fundamentals, without imposing overly restrictive limitations on speculative position holdings, which would impair market liquidity and reduce the hedging and price discovery functions of commodity exchanges?<sup>32</sup>

<sup>30</sup> Speculative position limits define the maximum position, either net long or net short, in one commodity futures (or options) contract, or in all futures (or options) contracts of one commodity combined, that may be held or controlled by one person other than a person eligible for a hedge exemption. UNCTAD, *The Global Economic Crisis*: 36.

<sup>31</sup> Swap dealers typically sell over-the-counter swaps to their customers (and hedge their price exposures with long futures positions in commodities. Swap dealers are generally included in the category “commercial traders” – exempted from regulation regarding speculative position limits. UNCTAD, *The Global Economic Crisis*: 36–37.

<sup>32</sup> UNCTAD (2009). *The Global Economic Crisis: Systemic Failures and Multilateral Remedies*. New York and Geneva: United Nations, 2009.

(e) Can we identify or design technically workable mechanisms in the present context of deregulated markets? How can we harness the momentum created by the crisis for change before we lose the sense of urgency for reforms?

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